

REPORT OF THE AUDITOR-GENERAL TO THE NORTERN CAPE PROVINCIAL LEGISLATURE AND THE COUNCIL ON MAGARENG LOCAL MUNICIPALITY

REPORT ON THE FINANCIAL STATEMENTS

Introduction

1. I have audited the financial statements of the Magareng local municipality set out on pages XX to XX, which comprise the statement of financial position as at 30 June 2013, the statement of financial performance, statement of changes in net assets, the statement of comparison of budget and actual amounts and the cash flow statement for the year then ended, and the notes, comprising a summary of significant accounting policies and other explanatory information.

Accounting officer's responsibility for the financial statements

2. The accounting officer is responsible for the preparation and fair presentation of these financial statements in accordance with the South African Standards of Generally Recognised Accounting Practice (SA Standards of GRAP) and the requirements of the Municipal Finance Management Act of South Africa, 2003 (Act No. 56 of 2003) (MFMA) and Division of Revenue Act of South Africa, 2012 (Act No. 05 of 2012) (DoRA) and for such internal control as the accounting officer determines is necessary to enable the preparation of financial statements that are free from material misstatement, whether due to fraud or error.

Auditor-General's responsibility

3. My responsibility is to express an opinion on these financial statements based on my audit. I conducted my audit in accordance with the Public Audit Act of South Africa, 2004 (Act No. 25 of 2004) (PAA), the *General Notice* issued in terms thereof and International Standards on Auditing. Those standards require that I comply with ethical requirements and plan and perform the audit to obtain reasonable assurance about whether the financial statements are free from material misstatement.
4. An audit involves performing procedures to obtain audit evidence about the amounts and disclosures in the financial statements. The procedures selected depend on the auditor's judgement, including the assessment of the risks of material misstatement of the financial statements, whether due to fraud or error. In making those risk assessments, the auditor considers internal control relevant to the entity's preparation and fair presentation of the financial statements in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the entity's internal control. An audit also includes evaluating the appropriateness of accounting policies used and the reasonableness of accounting estimates made by management, as well as evaluating the overall presentation of the financial statements.
5. I believe that the audit evidence I have obtained is sufficient and appropriate to provide a basis for my qualified audit opinion.

Basis for qualified opinion

Revenue from non-exchange transactions

6. I was unable to obtain sufficient appropriate audit evidence for revenue from property rates as the municipality had an inadequate system of internal control to account for revenue and keep proper record of all revenue charged. I was unable to confirm the amount disclosed by alternative means. Consequently, I was unable to determine whether any adjustments relating to revenue from non-exchange transactions stated at R3 616 610 (2012: R3 530 073) in the financial statements were necessary.

Additionally, there is a consequential impact on the surplus for the period and the accumulated surplus.

Revenue from exchange transactions

7. I was unable to obtain sufficient appropriate audit evidence for revenue from service charges as the municipality had an inadequate system of internal control to account for revenue and keep proper record of all revenue charged. I was unable to confirm the amount disclosed by alternative means. Consequently, I was unable to determine whether any adjustments relating to revenue from exchange transactions stated at R20 855 453 (2012: R17 847 186) in the financial statements were necessary. Additionally, there is a consequential impact on the surplus for the period and the accumulated surplus.

Expenditure

8. I was unable to obtain sufficient appropriate audit evidence for expenditure transactions relating to repairs and maintenance, bulk purchases and general expenditure as the municipality did not have adequate systems in place to maintain records of expenditure transactions. I was unable to confirm the amount disclosed by alternative means. Consequently, I was unable to determine whether any adjustments relating to expenditure transactions stated at R29 781 776 (2012: R26 143 456) in the financial statements were necessary. Additionally, there is a consequential impact on the surplus for the period and the accumulated surplus.

Receivables

9. I was unable to obtain sufficient appropriate audit evidence for the balances disclosed for consumer debtors. I was unable to confirm these receivables by alternative means. Consequently, I was unable to determine whether any further adjustments to consumer debtors stated at R4 614 552 (2012: R2 253 405) in the financial statements were necessary. Additionally, there is a consequential impact on the debt impairment in the statement of financial performance, surplus for the period and the accumulated surplus.

Payables from exchange transactions

10. I was unable to obtain sufficient appropriate audit evidence for payables from exchange transactions as the municipality could not provide all the required supporting documentation. I was unable to confirm the amount disclosed by alternative means. Consequently, I was unable to determine whether any adjustments relating to payables from exchange transactions at R46 879 924 (2012: R37 867 046) in the financial statements were necessary. Additionally, there is a consequential impact on the surplus for the period and the accumulated surplus.

Irregular expenditure

11. I was unable to obtain sufficient appropriate audit evidence for irregular expenditure as the municipality could not provide all the required supporting documentation. I was unable to confirm the amount disclosed by alternative means. Consequently, I was unable to determine whether any adjustments relating to irregular expenditure stated at R2 486 655 (2012: R229 601) in the financial statements were necessary.

Distribution losses

12. Distribution losses for water and electricity was not disclosed, as required by section 125(2d)(i) of the Municipal Finance Management Act. I could not determine the amount of these losses as it was impracticable to do so.

Unauthorised expenditure

13. The unauthorised expenditure disclosed as R1 474 724 in note 40 to the financial statements was not calculated as per the definition of unauthorised expenditure as stipulated in the MFMA section 1. The effect on the separate financial statements was that unauthorised expenditure was understated by R6 730 265 (2012: R5 800 119).

Qualified opinion

14. In my opinion, except for the possible effects of the matters described in the Basis for qualified opinion paragraphs, the financial statements present fairly, in all material respects, the financial position of the Magareng local municipality as at 30 June 2013 and its financial performance and cash flows for the year then ended, in accordance with SA Standards of GRAP and the requirements of the MFMA and DoRA.

Emphasis of matters

15. I draw attention to the matters below. My opinion is not modified in respect of these matters.

Fruitless and Wasteful expenditure

16. As disclosed in note 41 to the financial statements, fruitless and wasteful expenditure to the amount of R565 302 (2012: R476 064) was incurred. The total amount of fruitless and wasteful expenditure recorded in the annual financial statements at 30 June 2013 amounted to R565 302 (2012: R476 064). The majority of fruitless and wasteful expenditure is due to interest on late payments made to suppliers.

Restatement of corresponding figures

17. As disclosed in note 38 to the financial statements, the corresponding figures for 30 June 2012 have been restated as a result of an error discovered during 2013 in the financial statements of Magareng Local Municipality at, and for the year ended, 30 June 2012.

Impairments

18. As disclosed in note 4 to the financial statements the municipality had receivables from consumer debtors totalling R74 422 896 (2012: R84 362 162). A provision of R74 422 896 (2012: R84 362 162).

Additional matters

19. I draw attention to the matters below. My opinion is not modified in respect of these matters.

Unaudited supplementary schedules

20. The supplementary information set out in appendix A to F does not form part of the financial statements and is presented as additional information. I have not audited these schedules and, accordingly, I do not express an opinion thereon.

Supplementary explanations of budget variances presented outside the financial statements

21. The supplementary explanations of budget variances contained in the Actual versus Budget (Revenue and Expenditure) for the year ended 30 June 2013, as referred to in Appendix E(1), do not form part of the financial statements. I have not audited these explanations and accordingly I do not express an opinion thereon.

REPORT ON OTHER LEGAL AND REGULATORY REQUIREMENTS

In accordance with the PAA and the *General Notice* issued in terms thereof, I report the following findings relevant to performance against predetermined objectives, compliance with laws and regulations and internal control, but not for the purpose of expressing an opinion.

Predetermined objectives

22. The annual performance report was not presented for audit and consequently my findings below are limited to the procedures performed on the strategic planning and performance management documents.

The information was assessed to determine whether performance indicators and targets are measurable (i.e. well defined, verifiable, specific, measurable and time bound) and relevant as required by the National Treasury's *Framework for managing programme performance information* (FMPPI).

The material findings are as follows:

Usefulness of information

23. The National Treasury *Framework for managing programme performance information* (FMPPI) requires that performance targets be specific in clearly identifying the nature and required level of performance. A total of 100% of the targets were not specific in clearly identifying the nature and the required level of performance. This was due to the fact that management was not aware of the requirements of the FMPPI.
24. The National Treasury *Framework for managing programme performance information* (FMPPI) requires that performance targets be measurable. The required performance could not be measured for a total of 100% of the targets. This was due to the fact that management was not aware of the requirements of the FMPPI.
25. The National Treasury *Framework for managing programme performance information* (FMPPI) requires that the time period or deadline for delivery be specified. A total of 100% of the targets of the targets were not time bound in specifying a time period or deadline for delivery. This was due to the fact that management was not aware of the requirements of the FMPPI.
26. The National Treasury *Framework for managing programme performance information* (FMPPI) requires that indicators/measures should have clear unambiguous data definitions so that data is collected consistently and is easy to understand and use. A total of 100% of the indicators were not well defined in that clear, unambiguous data definitions were not available to allow for data to be collected consistently. This was due to the fact that management was not aware of the requirements of the FMPPI.
27. The National Treasury *Framework for managing programme performance information* (FMPPI) requires that it must be possible to validate the processes and systems that produce the indicator. A total of 100% of the indicators were not verifiable in that valid processes and systems that produce the information on actual performance did not exist. This was due to the lack of key controls in the relevant systems of collection/collation/ verification/ storage of actual performance information.

Compliance with laws and regulations

28. I performed procedures to obtain evidence that the municipality has complied with applicable laws and regulations regarding financial matters, financial management and other related matters. My findings on material non-compliance with specific matters in key applicable laws and regulations as set out in the General Notice issued in terms of

the PAA are as follows:

Budgets

29. Expenditure was incurred in excess of the limits of the amounts provided for in the votes of the approved budget, in contravention of section 15 of the Municipal Finance Management Act.
30. Quarterly reports were not submitted to the council on the implementation of the budget and financial state of affairs of the municipality within 30 days after the end of each quarter, as required by section 52(d) of the Municipal Finance Management Act.
31. Sufficient appropriate audit evidence could not be obtained that monthly budget statements were submitted to the mayor, as required by section 71(1) of the Municipal Finance Management Act.

Annual financial statements, performance and annual reports

32. The 2011/12 annual report was not made public immediately after the annual report was tabled in the council, as required by section 127(5)(a) of the Municipal Finance Management Act.
33. Financial statements were not submitted for auditing within two months after the end of the financial year, as required by section 126(1)(a) of the Municipal Finance Management Act.
34. The financial statements submitted for auditing were not prepared in all material respects in accordance with the requirements of section 122 of the Municipal Finance Management Act. Material misstatements of non-current assets identified by the auditors in the submitted financial statements were subsequently corrected, but the supporting records that could not be provided resulted in the financial statements receiving a qualified audit opinion.
35. The 2011/12 annual report was not tabled in the municipal council within seven months after the end of the financial year, as required by section 127(2) of the Municipal Finance Management Act.
36. A written explanation was not submitted to council setting out the reasons for the delay in the tabling of the 2011/12 annual report in the council, as required by section 127(3) and 133(1)(a) of the Municipal Finance Management Act.
37. Oversight report, containing comments on the annual report, was not adopted by council within two months from the date on which the 2011/12 annual report was tabled, as required by section 129(1) of the Municipal Finance Management Act.
38. The council's oversight report on the 2011/12 annual report was not made public within seven days of its adoption, as required by section 129(3) of the Municipal Finance Management Act.

Audit Committees

39. The audit committee did not advise the council on matters relating to internal financial control and internal audits, risk management, accounting policies, effective governance, performance management and performance evaluation as required by section 166(2)(a) of the Municipal Finance Management Act.
40. The audit committee did not advise the council on matters relating to the adequacy, reliability and accuracy of financial reporting and information, as required by section 166(2)(a)(iv) of the Municipal Finance Management Act.
41. The audit committee did not advise the council on matters relating to compliance with legislation, as required by section 166(2)(a)(vii) of the Municipal Finance Management Act.

42. The audit committee did not review the annual financial statements to provide the council with an authoritative and credible view of the financial position of the entity, its efficiency and effectiveness and its overall level of compliance with legislation, as required by section 166(2)(b) of the Municipal Finance Management Act.
43. The audit committee did not respond to the council on the issues raised in the audit reports of the Auditor-General, as required by section 166(2)(c) of the Municipal Finance Management Act.
44. The audit committee did not meet at least four times a year, as required by section 166(4)(b) of the Municipal Finance Management Act.

Internal audit

45. The internal audit unit did not function as required by section 165(2) of the Municipal Finance Management Act, in that:
 - it did not prepare a risk-based audit plan and an internal audit programme for the financial year under review.
 - it did not report to the audit committee on the implementation of the internal audit plan.
 - it did not advise the accounting officer and/or report to the audit committee on matters relating to internal audit, internal controls, accounting procedures and practices, risk and risk management and loss control.
 - The internal audit unit did not advise the accounting officer and reported to the audit committee on matters relating to compliance with the Municipal Finance Management Act, the Division of Revenue Act and other applicable legislation, as required by section 165(2)(b)(vii) of the Municipal Finance Management Act.

HR Management

46. An approved staff establishment was not in place, as required by section 66(1)(a) of the Municipal Systems Act.
47. The municipal manager did not sign performance agreements, as required by section 57(2)(a) Municipal Systems Act.

Expenditure Management

48. Money owing by the municipality was not always paid within 30 days or an agreed period, as required by section 65(2)(e) of the Municipal Finance Management Act.
49. Reasonable steps were not taken to prevent unauthorised expenditure, irregular expenditure and fruitless and wasteful expenditure, as required by section 65(2)(a) of the Municipal Finance Management Act.
50. An effective system of expenditure control, including procedures for the authorisation, was not in place, as required by section 65(2)(a) of the Municipal Finance Management Act.
51. An adequate management, accounting and information system was not in place which accounted for payments made, as required by section 65(2) of the Municipal Finance Management Act.

Transfer of funds and/or conditional grants

52. Sufficient appropriate audit evidence could not be obtained that the allocation for the Integrated National electrification Programme (Municipal) Grant was utilised for purposes other than those stipulated in the grant framework, in contravention of section 16(1) of the Division of Revenue Act.

53. Sufficient appropriate audit evidence could not be obtained that the allocation for the Municipal Systems Improvement Grant was utilised for purposes other than those stipulated in the grant framework, in contravention of section 16(1) of the Division of Revenue Act.

Revenue management

54. An effective system of internal control for debtors and revenue was not in place, as required by section 64(2)(f) of the Municipal Finance Management Act.
55. Sufficient appropriate audit evidence could not be obtained that revenue due to the municipality was calculated on a monthly basis, as required by section 64(2)(b) of the Municipal Finance Management Act.

Financial Misconduct

56. Unauthorised Irregular and Fruitless and Wasteful expenditure incurred by the municipality was not investigated to determine if any person is liable for the expenditure, in accordance with the requirements of section 32(2) of the Municipal Finance Management Act.

Procurement

57. Goods and services with a transaction value of below R200 000 were procured without obtaining the required price quotations as required by SCM regulation 17(a) & (c).
58. Bid specifications were not always drafted by bid specification committees which were composed of one or more officials of the municipality as required by SCM regulation 27(3).
59. Invitations for competitive bidding were not always advertised for a required minimum period of days, as required by SCM regulation 22(1) & 22(2).
60. Construction projects were not always registered with the Construction Industry Development Board (CIDB), as required by section 22 of the CIDB Act and CIDB regulation 18.
61. Contracts and quotations were awarded to bidders who did not submit a declaration on whether they are employed by the state or connected to any person employed by the state, as required by SCM regulation 13(c).

Predetermined objectives

62. The IDP adopted by the municipality did not reflect and identify the municipal council's vision for the long term development of the municipality / a financial plan / the key performance indicators and targets, as required by sections 26 and 41 of the Municipal Systems Act.
63. The municipality did not afford the local community at least 21 days to comment on the final draft of its integrated development plan before the plan was submitted to council for adoption, as required by municipal planning and performance management regulation 15(3).
64. The municipal council did not review its integrated development plan annually in accordance with an assessment of its performance measurements in terms of section 41 to the extent that changing circumstances demanded, as required by section 34 of the Municipal Systems Act and Municipal planning and performance management regulation 3.
65. The performance management system of the municipality was not in line with the priorities, objectives, indicators and targets contained in its integrated development plan and did not clarify the roles and responsibilities of each role-player in the functioning of the system and did not determine the frequency of reporting and the lines of

accountability for performance and/or did not relate to the municipality's performance management processes and/or did not provide for procedures by which the system is linked to the municipality's integrated development planning processes, as required by section 38(a) of the Municipal Systems Act and/or Municipal planning and performance management regulation 7(2)(c/e/f/g).

66. The performance management system of the municipality did not provide for the monitoring of performance and for the measuring and review of performance at least once per year, with regard to each of those development priorities and objectives and against the key performance indicators and targets set, as required by section 41 of the Municipal Systems Act.
67. The performance management system of the municipality did not provide for taking steps to improve performance with regard to those development priorities and objectives where performance targets are not met, as required by section 41 (1)(d) of the Municipal Systems Act.
68. The municipality did not establish mechanisms to monitor and review its performance management system, as required by section 40 of the Municipal Systems Act.
69. Revisions to the service delivery and budget implementation plan were not approved by the council after the approval of the adjustments budget, as required by section 54(1)(c) of the Municipal Finance Management Act.
70. The accounting officer of the municipality did not by 25 January assess the performance of the municipality during the first half of the financial year, as required by section 72(1)(a)(ii) of the Municipal Finance Management Act .
71. The performance audit committee did not meet at least twice during the financial year, as required by Municipal planning and performance management regulation 14(3)(a).
72. The MPAC reviewed the quarterly internal audit reports as required by Municipal planning and performance management regulation 14(4)(a)(i).
73. The performance audit committee did not submit, at least twice during the financial year, an audit report on the review of the performance management system to the council, as required by Municipal planning and performance management regulation 14(4)(a)(iii).
74. The internal audit did not audit the results of performance measurements, as required by section 45(1)(a) of the Municipal Systems Act and Municipal planning and performance management regulation 14(1)(a).
75. The internal audit unit did not assess the functionality of the performance management system, as required by Municipal planning and performance management regulation 14(1)(b)(i).
76. The internal audit unit did not assess the extent to which the performance measurements were reliable in measuring the performance of the municipality on key and general performance indicators, as required by Municipal planning and performance management regulation 14(1)(b)(iii).
77. The internal audit unit did not audit the performance measurements on a continuous basis and/or submitted quarterly reports on their audits to the municipal manager and the performance audit committee, as required by Municipal planning and performance management regulation 14(1)(c).
78. The annual performance report for the financial year under review was not prepared as required by section 46 of the Municipal Systems Act and section 121(3)(c) of the Municipal Finance Management Act.

79. The municipality did not have and maintain effective, efficient and transparent systems of financial and risk management and internal controls as required by section 62(1)(c)(i) of the Municipal Finance Management Act.

Consequence management

80. Unauthorised, Irregular and fruitless and wasteful expenditure incurred by the municipality was not investigated to determine if any person is liable for the expenditure, in accordance with the requirements of section 32(2) of the Municipal Finance Management Act.

Internal control

81. I considered internal control relevant to my audit of the financial statements, annual performance report and compliance with laws and regulations. The matters reported below under the fundamentals of internal control are limited to the significant deficiencies that resulted in the basis for disclaimer of opinion, the findings on the annual performance report and the findings on compliance with laws and regulations included in this report.

Leadership

82. The accounting officer did not take appropriate action to address lack of discipline in the finance and supply chain management directorate, resulting in non-compliance with applicable legislation. This, in turn, resulted in irregular expenditure.
83. The chief financial officer did not sufficiently monitor the recording and reconciliation of the financial records. Sufficient control measures were not developed by the chief financial officer, in conjunction with his support team, to address the qualifications reported in the prior years as identified in the action plan.
84. The accounting officer did not regularly monitor management's compliance with laws, regulations and internally designed policies and procedures. As a result, significant non-compliance issues were noted

Financial and performance management

85. Finance staff had an insufficient understanding of the accounting framework. This contributed to the numerous qualifications in the financial statements of the municipality.
86. The financial statements were not properly reviewed for completeness and accuracy prior to submission for auditing. This resulted in many findings relating to incorrect disclosure.
87. Effective performance systems, processes and procedures and the management thereof have not been adequately implemented. The financial statements were also subject to material adjustments. Documentation supporting amounts disclosed in the financial statements and achievement of predetermined objectives targets disclosed in the annual report was not available

Governance

88. The financial statements were subject to material corrections resulting from the audit, which are attributable to the lack of risk assessment performed, weaknesses in the design and implementation of internal control in respect of financial management, and financial reporting and weaknesses in the information systems. This also resulted in some prior year audit findings not being addressed in certain instances.
89. The accounting officer did not prioritise the appointment of the performance audit committee and therefore a performance audit committee was not in operation during the

financial year. This also resulted in the committee not being able to fulfil all its responsibilities

90. The audit committee and internal audit did not provide governance services to the extent required by legislation.

Auditor-General.

Kimberley

19 May 2014



AUDITOR - GENERAL
SOUTH AFRICA

Auditing to build public confidence